

May 28, 2013

GLORIA L. FRANKLIN, CLERK  
U.S. BANKRUPTCY COURT  
NORTHERN DISTRICT OF CALIFORNIA



Signed and Filed: May 27, 2013

*Dennis Montali*

DENNIS MONTALI  
U.S. Bankruptcy Judge

UNITED STATES BANKRUPTCY COURT  
NORTHERN DISTRICT OF CALIFORNIA

In re ) Bankruptcy Case  
GABRIEL TECHNOLOGIES CORP., et al., ) No. 13-30340DM  
(No. 13-30341)  
Debtors. ) Chapter 11

MEMORANDUM DECISION ON MOTION FOR CONVERSION TO  
CHAPTER 7 OR APPOINTMENT OF A CHAPTER 11 TRUSTEE

I. INTRODUCTION

On April 3, 2013, Qualcomm Incorporated ("Qualcomm") filed a Motion By Qualcomm Incorporated, Pursuant To 11 U.S.C. § 1112 For Conversion To Cases Under Chapter 7 Or, In The Alternative, For Appointment Of A Chapter 11 Trustee, For Cause (the "Motion") (Docket No. 40). Debtors, Gabriel Technologies Corporation and Trace Technologies LLC ("Debtors"), opposed the Motion. The Official Committee of Unsecured Creditors ("Committee") filed a Statement Of Position opposing the Motion. The matter was fully briefed and argued before the court on May 17, 2013.

For the reasons explained below, the court will deny the Motion.

1 II. DISCUSSION<sup>1</sup>

2 On February 1, 2013, the United States District Court for the  
3 Southern District of California, in an action there by Debtors  
4 against Qualcomm and other defendants for misappropriation of  
5 intellectual property and related patent disputes (the "District  
6 Court Action"), entered an order directing Debtors to pay Qualcomm  
7 and the two other parties nearly \$12-1/2 million in attorneys'  
8 fees; after credit of an \$800,000 bond that had been posted in  
9 Qualcomm's favor, Debtors were ordered to pay the remaining amount  
10 of over \$11-1/2 million. That outcome and a judgment in favor of  
11 Qualcomm was the culmination in the District Court Action of  
12 expensive and extensive litigation initiated in 2008. Debtors are  
13 appealing that adverse judgment and the attorneys' fees award and  
14 stake their future in this Chapter 11 case on a successful appeal  
15 and thereafter a trial or some other favorable disposition. They  
16 were unable to obtain a bond to stay Qualcomm's enforcement of the  
17 attorneys' fees award although exactly what assets Qualcomm could  
18 reach is not evident.

19 When Debtors filed these Chapter 11 cases on February 14,  
20 2013, they had ceased all business operations, had no employees,  
21 no customers, no products, and no source of operating income. The  
22 schedules show tangible assets (office furniture) valued at \$200,  
23 cash of less than \$300 and a \$1500 lease deposit. What remains of  
24 any hope of a claim against Qualcomm has an unknown value and  
25 there is no mention of the potential claim against officers and  
26 directors mentioned below.

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28 <sup>1</sup> The following discussion constitutes the court's findings  
of fact and conclusions of law. Fed. R. Bankr. P. 7052(a).

1       The Motion, in short, urges that an independent trustee be  
2 appointed under either Chapter 7 or Chapter 11, so that the  
3 trustee may make an objective assessment of whether and if to  
4 continue to prosecute the appeal against Qualcomm, and whether and  
5 if to prosecute an action against former officers and directors of  
6 Debtors for initiating and unsuccessfully prosecuting the District  
7 Court Action. Qualcomm also has spent a great deal of time in its  
8 papers supporting the Motion to be highly critical of prior  
9 management of the Debtors, and to stress that the current  
10 management, along with the members of the Committee, are  
11 irreconcilably conflicted and should not be permitted to dictate  
12 the outcome of these Chapter 11 cases.

13       Debtors believe that they should remain in possession and be  
14 given an opportunity to seek confirmation of a Chapter 11 plan.  
15 To that end, on April 24, 2013, they filed Debtors' Joint Plan Of  
16 Reorganization (April 24, 2013) (the "Plan"), together with a  
17 draft [proposed] Disclosure Statement for the Plan. Qualcomm  
18 contends that the Plan is patently unconfirmable; Debtors and the  
19 Committee disagree. For purposes of ruling on the Motion, the  
20 court makes no determination on whether the Plan, or any variation  
21 of it, could be confirmed.<sup>2</sup> That will come later.

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25       <sup>2</sup> At the hearing on May 17, the court asked the Debtors'  
26 counsel about the possibility of deferring any consideration of  
27 the Plan while they prosecute their appeal. That suggestion was  
28 rejected, in part, because the Debtors believe they can obtain  
funding from a third party who desires confirmation of the Plan  
and is apparently willing to provide some sort financing to  
facilitate that outcome.

1 The Motion was brought under § 1112(b).<sup>3</sup> That subsection  
2 provides, in part:

3 **(b)(1)** Except as provided in paragraph (2) and  
4 subsection (c), on request of a party in interest, and  
5 after notice and a hearing, the court shall convert a  
6 case under this chapter to a case under chapter 7 or  
7 dismiss a case under this chapter, whichever is in the  
best interests of creditors and the estate, for cause  
unless the court determines that the appointment under  
section 1104(a) of a trustee or an examiner is in the  
best interests of creditors and the estate.

8 **(2)** The court may not convert a case under this chapter  
9 to a case under chapter 7 or dismiss a case under this  
10 chapter if the court finds and specifically identifies  
11 unusual circumstances establishing that converting or  
dismissing the case is not in the best interests of  
creditors and the estate, and the debtor or any other  
party in interest establishes that--

12 **(A)** there is a reasonable likelihood that a plan will be  
13 confirmed within the timeframes established in sections  
14 1121(e) and 1129(e) of this title, or if such sections  
do not apply, within a reasonable period of time; and

15 **(B)** the grounds for converting or dismissing the case  
16 include an act or omission of the debtor other than  
under paragraph (4)(A)--

17 **(i)** for which there exists a reasonable justification for the  
act or omission; and

18 **(ii)** that will be cured within a reasonable period of time  
fixed by the court.

19 \* \* \*

20 **(4)** For purposes of this subsection, the term 'cause'  
includes--

21 **(A)** substantial or continuing loss to or diminution of  
22 the estate and the absence of a reasonable likelihood of  
rehabilitation;

23 **(B)** gross mismanagement of the estate;

24 11 U.S.C. § 1112.

25 Qualcomm did not base the Motion on § 1104(a), which permits

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27 <sup>3</sup> Unless otherwise indicated, all chapter, section and rule  
28 references are to the Bankruptcy Code, 11 U.S.C. §§ 101-1532, and  
to the Federal Rules of Bankruptcy Procedure, Rules 1001-9037.

1 an appointment of Chapter 11 trustee or an examiner but does not  
2 deal with dismissal or conversion.

3 Conversion or dismissal is available under § 1112(b)(1) "for  
4 cause". The burden is on the moving party (Qualcomm) to establish  
5 cause. 7 COLLIER ON BANKRUPTCY, ¶ 1112.04 [4](Henry Sommers & Alan  
6 Resnick, 16th ed. 2009). "Thus, until the movant carries this  
7 burden, the statutory direction that the court 'shall convert the  
8 case to a case under chapter 7 or dismiss the case' is not  
9 operative." *Id.*

10 Section 1112(b)(4) enumerates sixteen different and  
11 nonexclusive illustrations of cause. For purposes of this Motion,  
12 the only two of those sixteen alternatives urged by Qualcomm are  
13 found in § 1112(b)(4)(A), "substantial or continuing loss to or  
14 diminution of the estate and the absence of a reasonable  
15 likelihood of rehabilitation" and § 1112(b)(4)(B), "gross  
16 mismanagement of the estate." Qualcomm has not carried its  
17 burden of establishing cause under either alternative.

18 Because the debtor has no tangible assets or realizable value  
19 and no operations, there has not been and is no "substantial" loss  
20 or diminution of the estate. Simply stated, there is nothing left  
21 to lose. The question then becomes whether accrual of fees of  
22 professionals employed by the Debtors and the Committee, and the  
23 possibility of additional Delaware state taxes, amount to the type  
24 of "continuing loss" that Congress had in mind to trigger the  
25 nearly mandatory conversion, dismissal or chapter 11 trustee  
26 options § 1112(b)(1) contemplates.

27 Perhaps from an accounting perspective (profit and loss),  
28 such accruals would constitute such losses. But the accrual of

1 liabilities are not the same as the incurring of actual out-of-  
2 pocket losses, such as the dissipation of assets that diminishes  
3 the estate. Leaving the Debtors in possession of the chapter 11  
4 estate is not risking some ever-diminishing pool of assets.<sup>4</sup>

5 Even if that were the case, the court must consider how long  
6 a situation must persist to be said to be continuing for purposes  
7 of § 1112(b)(4)(A). These jointly administered cases are just  
8 over three months along and the Debtors have already filed the  
9 Plan that will be tested very soon. The accrual of liabilities  
10 (losses) will end soon, either with a confirmed joint plan or  
11 conversion to chapter 7, a point conceded by Debtors' counsel to  
12 be inevitable if confirmation is denied. Thus, even if there is  
13 any continuing loss at all, it will not be continuing very long at  
14 all.

15 Because § 1112(b)(4)(A) uses the conjunctive (loss and  
16 absence of likelihood of rehabilitation) the court does not need  
17 to deal with the thorny question of whether "absence of a  
18 reasonable likelihood of rehabilitation" applies to debtors whose  
19 only hope is a successful appeal of an adverse litigation result  
20 and retrial, and has no going concern or business to rehabilitate.

21 The only other "cause" trigger under § 1112(b)(4) is the  
22 gross mismanagement of the estate under § 1112(b)(4)(B). Qualcomm  
23 is long on rhetoric about the potential conflicts that it believes  
24 infect current management but it has not provided any proof of

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26 <sup>4</sup> One court has even suggested that where the debtor is not  
27 an operating company, but merely holds an intangible asset, the  
28 loss - diminution factor is not even relevant. In re 3 Ram, Inc.,  
343 B.R. 113, n. 14 (Bankr. E.D. Pa. 2006) (but case dismissed  
because proposed plan was not feasible and feasible plan not  
possible).

1 specific mismanagement in the short time Debtors have been in  
2 control of the estate. It has not established cause under that  
3 alternative.

4 The Plan, or some variation of it, may or may not be  
5 confirmable, and Debtors and the Committee will have to deal with  
6 anticipated objections to confirmation that Qualcomm will likely  
7 make. That is for another day. On the face of it, the court  
8 cannot say that the Plan is unconfirmable as a matter of law.  
9 What the court can say, however, is that if Debtors do not obtain  
10 confirmation within the timetable to be set, Qualcomm will have  
11 its wish, albeit under § 1112(b)(4)(J) ("failure to file a  
12 disclosure statement, or to file or confirm a plan, within the  
13 time fixed ... by order of the court;").

### 14 III. CONCLUSION

15 For the foregoing reasons, the court will deny the Motion by  
16 a separate order being issued concurrently with this Memorandum  
17 Decision. The court will conduct a Status Conference on June 10,  
18 2013, at 1:30 p.m., at which time it will set a tight schedule for  
19 consideration of a final disclosure statement to accompany either  
20 the Plan or any revised plan Debtors may file before then.  
21 Debtors' counsel is directed to meet and confer with the  
22 Committee's counsel and with Qualcomm's counsel to discuss any  
23 necessary discovery prior to consideration of the disclosure  
24 statement and further to discuss a time table for a hearing on  
25 approval of the final disclosure statement and confirmation of the  
26 Plan or any other plan that may be filed. The court expects those  
27 hearings to be concluded by the end of August, 2013.

28 \*\*END OF MEMORANDUM DECISION\*\*

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